140

CONTROLLERS' CONGRESS

OF THE

NATIONAL
RETAIL DRY GOODS
ASSOCIATION

OFFICIAL PUBLICATION

VOL. I—DESCRIPTIVE TEXT

A STANDARD METHOD OF ACCOUNTING FOR RETAIL STORES

FINANCIAL STATEMENTS

OPERATING STATEMENTS

CLASSIFICATION AND
DISTRIBUTION OF EXPENSE

CLASSIFICATION
OF MERCHANDISE

200 FIFTH AVE., NEW YORK CITY

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AMPLIFYING AND REVISING "THE CLASSIFICATION AND DISTRIBUTION OF EXPENSE IN RETAIL STORES" ISSUED BY THE NATIONAL RETAIL DRY GOODS ASSOCIATION IN 1917.

200 5th AVE., NEW YORK CITY

CONTENTS

INTRODUCTION

Diversity in accounting methods and confusion in terminology among retail stores have brought retail merchants to the realization that the adoption of standard methods is essential, if the scientific study of the function of retail distribution is to keep pace with the development of scientific methods in other branches of commerce.

The tendency among retail stores has been to devise new and better systems only as the growth and progress of each business demanded improved routine. The need for standard processes has become more apparent as merchants compare their results with one another. During the past few years when trade associations, or government agencies, have sought comparative statistics from retailers, it has been found extremely difficult to tabulate, accurately, the information obtained, however freely it was furnished, because of the lack of uniformity in the terms used, and the methods employed.

The modern tendency of the government is to require increasingly detailed reports covering the operation of all business enterprises. Out of the need of having such reports on a comparable basis has arisen government prescription of accounting methods in other branches of industry. It is obvious that lines of business which have not voluntarily adopted a uniform system of accounts, acceptable to the government, may have such system required by those less familiar with retail problems. This plan of standardization has been prepared in anticipation of a need which may arise eventually.

Aside from the sheer practical necessity for standardization there are other equally important reasons for introducing uniform accounting practice among the craft. Trained accountants, entering the retail field for the first time, are bewildered by the diversity of practice. An accepted standard will not only assist the expert in more quickly adapting himself to retail problems, but will be an important factor in training the intelligent beginners within the retail field itself.

Every enterprising merchant looks forward to the time when his business will have become a larger institution with ever widening sphere of influence. With the standard classification before him he may adjust his accounting system to the greater detail necessary in the larger operation without seriously disturbing the comparison of previous years.

It is of even greater importance to the retailer to have a more thorough knowledge of his business, and a record of facts which he can compare with his fellow-merchant. From these comparisons will be developed new standards or measures of performance by which merchants may determine accurately the degree of their own success.

The report is presented in two volumes—Volume I, the Descriptive Text, and Volume II, the Charts, which will enable the reader to have before him, at the same time, both text and charts.

The explanatory text and bookkeeping procedure provided in this volume will assist in the interpretation and application of the Classification described in the Charts contained in Volume II.

PUBLICATION

This publication is printed by authority of the Board of Directors of the Controllers' Congress and the National Retail Dry Goods Association.

The issuing of this publication was made possible by the efforts of the following individuals and courtesy of their respective companies.

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PART I

BALANCE SHEET

The Balance Sheet consists of account balances remaining open on the ledger after the balances of income and expense accounts have been transferred to Profit and Loss Account, and the resultant balance of that account to Surplus or Investment Account, or after the effect of such a closing of the books has been produced by consolidating those accounts in memoranda only. It thus represents the condition of affairs at a fixed moment of time, denoting **position** as contrasted with the Operating Statement (Income Sheet), which denotes **progress.**

The balances are listed under two principal captions, "Assets," appearing on the left-hand side of the page, "Liabilities," on the right. Broadly speaking, it may be said that the assets represent the property of the business, the liabilities, the extent of ownership thereof or interest therein. The assets are a classified list of things of value, exhibited with due regard to the liquidity of the various classes. The liabilities are a classified list of ownerships or interests with due regard to the priority of their respective claims to the assets.

BALANCE SHEET ACCOUNTS

ASSETS

CURRENT

CASH

On Hand

For deposit
Cashiers' funds

On Deposit

Bank accounts (an account with each bank, or one account with a subsidiary bank register.)

NOTES RECEIVABLE

Customers' notes
Accrued interest
Reserve for possible losses (contra)

ACCOUNTS RECEIVABLE

Charge
C. O. D.
Layaway or Will-calls
Installment and Mortgage
Reserve for possible losses (contra)

MERCHANDISE

Inventory of merchandise on hand
Merchandise paid for in advance

U. S. SECURITIES

Bonds (an account with each issue)
Certificate of indebtedness
Accrued interest
War savings stamps
Reserve for possible losses (contra)

OTHER ASSETS

Securities owned (An account with each classification or issue)
Accrued interest
Stocks owned (An account with each classification or issue)
Notes receivable—Current and non-current
Accrued interest
Insurance deposits
Cash surrender value of life insurance policies
Common carrier claims
Land and buildings—Not used in the operation of the business
Personal accounts (A separate account with each individual)

DEFERRED CHARGES

Unexpired insurance premiums
Prepaid interest on notes payable
Supply inventory
Prepaid expenses (An account with each classification)
Organization expenses

PERMANENT

Land
Leasehold and improvements to leased buildings
Reserve for amortization of lease (contra)
Buildings
Reserve for depreciation (contra)
Machinery and equipment
Reserved for depreciation (contra)
Store furniture and fixtures
Reserve for depreciation (contra)
Office furniture and equipment
Reserve for depreciation (contra)
Delivery equipment
Reserve for depreciation (contra)

GOOD WILL, PATENTS AND TRADEMARKS

LIABILITIES

CURRENT

NOTES PAYABLE

For money borrowed from banks
For money borrowed through brokers
For money borrowed from officers
For money borrowed from others
For purchases
Trade acceptances

ACCOUNTS PAYABLE

For merchandise and expense purchases
For federal sales taxes
For unredeemed cash refunds
For unredeemed gift certificates
Leased section accounts (An account with each section)
Personal accounts (An account with each individual)

ACCRUED ACCOUNTS

Taxes, Real and Personal—City, County and State
Pay roll
Interest on notes payable
Rent
Expenses (An account with each classification)

FUNDED INDEBTEDNESS

Mortgages
Bonds (an account with each classification or issue)

RESERVES

For federal income taxes
For contingencies

PROPRIETARY INTERESTS
(If a Corporation)

CAPITAL STOCK

Preferred—Authorized
Less: Unissued
Common—Authorized
Less: Unissued

PROFIT AND LOSS—SURPLUS

Surplus
Undivided profits

(If a partnership or sole proprietorship)

INVESTMENT ACCOUNTS

An account with each partner

PROFIT AND LOSS—CURRENT ACCOUNT

ASSETS

The following divisions are provided to set forth the nature and comparative degree of liquidity of the various classes of Assets.

CURRENT ASSETS

Current Assets consist of Cash and those items which may be readily converted into cash and are continually changing through the carrying on of the business. Usually these consist of Cash, Notes and Accounts Receivable, Inventories and Government Securities.

CASH

This account represents the balance of cash on hand and in banks at the date of the Balance Sheet.

NOTES RECEIVABLE

This account represents the face value of all evidences of indebtedness (except as below provided) which are the property of the business and which are considered collectible. This account does not include investments, for which other provision has been made.

ACCOUNTS RECEIVABLE

This account includes all amounts owing to the business upon accounts with solvent trade debtors, except claims evidenced by notes, etc., provided for in the preceding account.

MERCHANDISE .

This account includes the cost or market value, whichever is the lower, of merchandise on hand, purchased for resale and merchandise paid for in advance, in the regular course of business. For full discussion, see text accompanying item No. 13, "Inventory at End of Period," on the Operating Statement.

U. S. SECURITIES

This account represents the cost or market value, whichever is the lower, of United States Government Securities on hand at date of Balance Sheet.

OTHER ASSETS

All other Assets have been provided for under this group, such as securities of other corporations and sundry notes and accounts receivable, other than those arising in the ordinary transactions of the business.

DEFERRED CHARGES

This group of accounts consists of expenses paid in advance, chargeable to subsequent periods, and to this extent represent an Asset. They include the prepayment of Insurance, Taxes, Rent, Supplies and Organization Expenses.

PERMANENT ASSETS

This item represents the cost of all interests in land, buildings, leaseholds, machinery, fixtures and equipment on hand at the date of Balance Sheet, with proper provision for depreciation, obsolescence and amortization thereof.

GOOD WILL, PATENTS AND TRADEMARKS

This account represents the cost or amortized valuation of any assets acquired, which can be classified under this caption.

LIABILITIES

The following divisions are provided to set forth the nature of the various classes of Liabilities and the priority of their respective claims against the Assets.

CURRENT LIABILITIES

Current Liabilities consist of notes and accounts payable, and of items accrued in anticipation of payment.

NOTES PAYABLE

This item represents the amount of indebtedness evidenced by notes at the date of the Balance Sheet, except funded debts.

ACCOUNTS PAYABLE

This item represents all Liabilities incurred by the business upon open accounts.

ACCRUED LIABILITIES

This item represents the amount of liabilities accrued, and consists of such items as taxes, payroll, interest, rent, advertising, traveling expenses, water and other services, which have been rendered the business previous to the date of the Balance Sheet, but which on that date are not due and are unpaid, and for which no invoice has been rendered.

FUNDED INDEBTEDNESS

This item represents the long term indebtedness of the business, and has been divided into mortgages and bonds.

RESERVES

This account represents the amount of surplus set aside for federal income taxes, contingencies and the liquidation of losses not otherwise provided for, or other items the actual amount of which are not determinable at the date of the Balance Sheet.

CAPITAL STOCK

This account represents the amount of stock authorized, having a par value, less the par value of redeemed or unissued stock. In the case of stock issued of no par value, it represents the cash, or its equivalent, received in payment of stock issued.

The purchases of its own stock by a corporation should be carried as "Treasury Stock," under other assets. The laws of the various states are not uniform in regard to the retirement of stocks, and Treasury Stock should be treated accordingly.

PROFIT AND LOSS—SURPLUS

This account represents the amount of paid-in surplus and the undistributed earnings of the business at the date of the Balance Sheet.

CAPITAL OR INVESTMENT ACCOUNTS

These accounts represent the net investment at the date of the Balance Sheet of the partners or sole proprietorship of a business not incorporated.

PROFIT AND LOSS—CURRENT

This account represents the net profit or loss of the business for the current period.

PART II

OPERATING STATEMENT

INCOME (1)

Caption only.

SALES (2)

Caption only.

GROSS SALES (3)

The total of all sales as defined under "Definitions," less any discounts granted to customers or employees, but before any returns or allowances are taken into account, constitute the **Gross Sales** of the business.

Gross Sales is the first item on the Operating Statement because it is the natural point of departure for a logical analysis of profit and loss, the negotiation of sales at a favorable rate being the principal business of, and source of profit to, the retailer.

This account should be credited at selling price with all sales of merchandise purchased for resale at a profit, of merchandise manufactured in whole or in part by the retailer for sale at a profit, with alteration charges collected from customers and receipts of restaurants and personal service departments, and only those.

Specifically, it should not include sales which are in effect reclamations of expense such as sales of waste paper, sales which are in effect reductions of assets other than merchandise, such as sales of discarded fixtures or other equipment, or interdepartmental transfers of merchandise which are reductions of inventory in the department issuing and either increases in inventory in the department receiving or additions to an asset or expense account. Neither should it include excise taxes collected from customers, as these should be reserved until their due date in specific liability accounts, one for each class of tax.

Amounts charged customers for transportation of merchandise to distant points should not be included in **Gross Sales,** but should be treated as a reduction of expense.

This account may, and should be, subdivided into its constituent elements, Gross Cash Sales, Gross Charge Sales and Gross C. O. D. and Layaway or Will Call Sales. These in turn should be shown by departments in a subsidiary record if the business is departmentized.

GROSS SALES—LEASED SECTIONS (5)

Gross Sales from leased sections should be shown separately on this line.

There is good reason for this position. Leased Section operations are similar in kind to the operations which are the stores principal line of activity. The profits which accrue from them are mainly profits on the sale of merchandise at retail, although that merchandise is not the property of the store. This being the case, it is preferable to exhibit such profits in a position where they can be readily combined with the merchandising profits on own goods to give a total which is representative of the profits on all sales at retail within the same store rather than to include them with Other Income.

RETURNS AND ALLOWANCES (4)

This account furnishes the means of exhibiting separately the effect upon the business of goods returned for credit by customers and allowances made to them during the period.

No other reductions from Gross Sales should be included in the classification. Specifically, customers' and employees' discounts should not be charged here, as they have already been deducted from the sale, and such sales are therefore net when credited to Gross Sales.

In considering returns and allowances, it must be borne in mind that the expenses of the business are in large part determined by the volume of Gross Sales. Consequently, returns and allowances represent a loss greater than that involved in the mere cancellation or reduction of selling price previously credited to Gross Sales. They reflect in addition an element of expense which produces no immediate return and which must necessarily be included as a cost of obtaining the sales which "stay sold."

RETURNS AND ALLOWANCES—LEASED SECTIONS (6)

Returns and Allowances of leased sections should be shown separately on this line.

NET SALES (7)

This is the principal income item out of which must be met all items of cost or expense. This being the case, it is taken as 100%, or the figure upon which all subsequent percentages are calculated.

COST OF SALES (8)

INVENTORY AT BEGINNING OF PERIOD (9)

This item on the Operating Statement of any fiscal period corresponds exactly with item 13 on the Operating Statement of the preceding period. A full discussion will be found under item 13.

PURCHASES—NET (10)

This account is debited in the first instance with the invoice cost of all merchandise purchased for resale, less trade discounts which are an integral part of the purchase price, but before deducting cash discounts which are conditional upon the date of settlement.*

Purchases should be charged both with the cost of materials bought for manufacturing departments and with the manufacturing payroll and other expense.

Transfers to a selling department should be made at total cost, the selling department taking credit for sales, when made, at full retail price. The selling departments thus absorb the operations of the manufacturing departments completely.

Import duties and other charges on foreign merchandise, such as commissionnaires' fees, insurance, etc., are a part of the cost of such merchandise and should be charged to Purchases.

This account is credited with all merchandise returned to manufacturers and with all allowances received from them on account of unsatisfactory merchandise.

FREIGHT, EXPRESS AND CARTAGE INWARD (11)

This account is charged with all inward transportation costs since they are demonstrably an additional cost of merchandise rather than an expense.

From the merchandise standpoint, the delivered cost of his goods is what a merchant needs most to know in determining the retail price at which he will mark them. The cost of identical goods to merchants located at different distances from the central market is not the same and mark-up comparisons between them will be misleading unless the variable factor of transportation is included in their merchandise costs.

*In some businesses, there is set up a standard rate of cash discount which the departments are required to obtain on their purchases. In case they do not obtain it, they are charged with the difference between the required discount and the discount allowed, or available discount so-called. It is not to be understood that the Committee recommends this practice, but, where it is followed, it is recommended that this difference, commonly called "Loading," be charged to purchases, since credit for all cash discounts, whether they be actually obtained from the manufacturer or charged to departments, is taken only after Gross Cost of Merchandise Sold, item 14, is arrived at, appearing in Discount Earned on Merchandise Purchases, item 15.

From the expense standpoint, transportation costs are not responsive to management policies as are the controllable expenses, such as wages and advertising. Neither are they relatively fixed in amount as are other expenses, such as rent, etc. In fact, they are quite unlike the expenses of the business in that they are entirely dependent and consequent upon the movement of merchandise inward, fluctuating in exact proportion to the volume of goods received. Therefore, aside from the incorrectness of including them in expenses, it would be inexpedient to do so, if only for the reason that expenses would thereby be increased by an element which the expense management could not control and for which it could not be held responsible.

Inventory treatment of this item will be dealt with under item 13, Inventory at End of Period.

TOTAL INVENTORY AND PURCHASES (12)

This item is **Inventory at Beginning of Period** plus **Purchases—Net,** and **Freight, Express and Cartage Inward.**

INVENTORY AT END OF PERIOD (13)

Inventory at End of Period should be the inventory of merchandise on hand, taken at cost or market, whichever is lower. This conforms to the best accounting practice and is in accord with the requirements of the Treasury Department which permits either of two methods; i. e., (a) cost, or, (b) cost or market, whichever is lower, provided the same method is followed in subsequent years. In the retail business, certainly, the latter method is the more conservative, in fact, it is the only safe one to follow if an overstatement of profits is to be avoided.

Now, under the Retail Inventory Method, depreciation is automatically taken into account through markdowns, so that the inventory at end of the period is really depreciated inventory.

This is not the case under the cost inventory method, where, by use of a code system, the inventory is figured at billed cost. Under that method, the utmost care must be exercised to see that the figure used is either cost or market, whichever is lower, if the merchant is following that method. The instructions are specific and only one of these two figures will be permitted by the government. The depreciation which the merchant who operates under the retail inventory method obtains automatically is denied to the merchant who operates under the cost method, inasmuch as the burden of proof is on him to substantiate that any figure other than cost used in his inventory is an actual market figure at inventory time—that is, it is offered for sale in the ordinary wholesale market at the rate at which the inventory is taken. Only one exception to this rule is made in favor of the merchant who operates on the cost inventory method. This exception is, that, where the retail price at inventory time is less than the cost price originally paid for an article, the retail price may be used as cost in inventory.

Under the Cost Inventory Method, therefore, inventory at end of period should consist of:

(a) Merchandise on hand at (a) cost, or (b) cost or market, whichever is lower, according to the method used by the merchant. Materials on hand in manufacturing departments should be included.

(b) Average rate of Freight, Express and Cartage Inward for the period, wherever the figure is obtainable, applied to (a).

(c) Manufacturing payroll and materials involved in work in process, unfinished jobs which have not been transferred from a manufacturing to a selling department.

(Note) The amount obtained by applying to (a) above the average rate of Discounts Earned on Merchandise Purchases, item 15, should be deducted from item 15.*

Under the Retail Inventory Method, recommended by the Association and approved by the Treasury Department, inventory at end of period should consist of:

(a) The cost equivalent of the retail value of the merchandise on hand. This cost equivalent is obtained by applying to the retail value of the inventory the complementary cost rate of the average percentage of purchase mark-up; i. e., the percentage rate reached by subtracting the latter from 100% (see complete description of the Retail Inventory Method under Definitions).

*Where the practice of charging to purchases the difference between required and available discounts is followed, the average rate of such difference applied to (a) is a proper addition to the inventory itself.

(b) Materials on hand in manufacturing departments.

(c) Manufacturing payroll and materials** involved in work in process, unfinished jobs which have not been transferred from a manufacturing to a selling department.

(NOTE) The amount obtained by applying to (a) above the average rate of Discounts Earned on Merchandise Purchases, item 15, should be deducted from item 15.

GROSS COST OF MERCHANDISE SOLD (14)

This item is **Total Inventory and Purchases** less **Inventory at End of Period.**

DISCOUNT EARNED ON MERCHANDISE PURCHASES (15)

Some businesses treat their cash discounts on merchandise purchases as a reduction of the cost of those purchases, while others consider them as "Other Income" and credit them as such at the bottom of the Operating Statement after Net Operating Profit (or Loss) is determined.

The opposing views are presented in the discussion on Discounts under Customs and Usages and, therefore, will not be dealt with here. Suffice it to say that there is a decided division of opinion which necessitates the accounting treatment of this item as shown on the Operating Statement. The location of item 15 permits of either application. The merchant who has operated on an "Other Income" basis for discounts may take item 14, Gross Cost of Merchandise Sold, add thereto item 17, Alteration Costs, to obtain a working "Cost of Sales" for the purpose of controlling his department managers as formerly, and for that purpose alone. It must always be clearly borne in mind, however, that the "Cost of Sales" so arrived at is for internal management purposes only and is not Cost of Sales as defined in this report under item 26. Regardless of discount treatment for departmental control, item 26 should be calculated, as should all the items on the Operating Statement, in accordance with instructions in order to serve the main object of this program of standardization; i. e., a common basis for comparison of the operating reports of retail stores. This account, therefore, consists of—(a) Discounts Earned on Merchandise Purchases, LESS, (b) amount obtained by applying average rate of (a) above to value of merchandise on hand. (See item 13.) The amount so deducted should be carried over into the next fiscal period in a reserve account, the entry then being reversed.

NET COST OF MERCHANDISE SOLD (16)

This item is **Gross Cost of Merchandise Sold** less **Discount Earned on Merchandise Purchases.**

ALTERATION COSTS (17)

This item represents cost of alteration sales included in Gross Sales, item 3.

Materials used, wages and other expenses of alteration rooms should be included here. The sum of these items constitutes an additional cost of merchandise, since a sale in which alterations are involved is not complete until they are finished and accepted by the purchaser. In so far as the position of this item on the Operating Statement is concerned, there is a distinction between the costs which it represents and the other additions to merchandise cost. Item 11, Freight, Express and Cartage Inward, represents an additional cost incurred in the movement of merchandise inward and the placing of it in stock while the costs represented by item 17 do not originate until the merchandise begins to move outward.

MERCHANDISE COSTS—OWNED DEPARTMENTS (18)

This item is **Net Cost of Merchandise Sold** plus **Alteration Costs.**

MERCHANDISE COSTS—LEASED DEPARTMENTS (19)

This item represents the cost of sales before considering expenses in leased sections as reflected in special ledger account.

**The reason for treating manufacturing pay-roll and materials separately is that it is inadvisable to attempt to include manufacturing departments in the percentage of purchase mark-up calculation under the Retail Inventory Method. The chief difficulty lies in the fact that there is a fundamental difference between charges to Purchases for a Selling Department and those for a Manufacturing Department. When purchases for a selling department are entered at cost and retail in the stock records, the marked-up price or Retail is placed on the merchandise tag attached to the merchandise and in consequence there is a basis of comparison at retail between merchandise and stock records at inventory time.

But, when pay-roll and materials are charged to Purchases against a manufacturing department, it is not known in what finished form they will be worked up nor at what retail that finished form will sell. Consequently, any mark-up placed upon them would be only an estimate, the correctness of which there would be no subsequent opportunity of verifying since it would have been applied in bulk while the finished product would be transferred by the job or piece

***TOTAL MERCHANDISE COSTS (20)**

This item is the total of items 18 and 19.

OPERATING EXPENSES—OWNED DEPARTMENTS (21)

This item represents a class of accounts so important that they merit special treatment and have received it elsewhere in this report in the study entitled "Classification and Distribution of Expense." For the purposes of the Operating Statement, it is sufficient to say, that the caption of this item covers all expenses of the business, whether direct or indirect, which are chargeable to owned departments.

OPERATING EXPENSES—LEASED DEPARTMENTS (22)

This item represents expenses similar to those discussed under item 21, but chargeable to leased departments.

OPERATING EXPENSES—TOTAL (23)

This item is the total of items 21 and 22.

COST OF SALES—OWNED DEPARTMENTS (24)

This item is **Merchandise Costs—Owned Departments** plus **Operating Expenses—Owned Departments.**

COST OF SALES—LEASED DEPARTMENTS (25)

This item is **Merchandise Costs—Leased Departments** plus **Operating Expenses—Leased Departments.**

COST OF SALES—TOTAL (26)

This item is the total of items 20 and 23 and also of items 24 and 25.

OPERATING PROFIT OR LOSS (27)

This item is **Net Sales** (item 7) less **Cost of Sales—Total** (item 26)

OTHER INCOME AND LOSSES (28)

Caption only.

OTHER INCOME (29)

This item represents non-operating income from sources other than the ordinary operations of the business as represented by the preceding items. The following are typical "Other Income" accounts.

CREDITS

RENT CHARGED TO DEPARTMENTS........	....	
LESS: RENT PAID OR ACCRUED........	....	
RENTAL PROFIT........		....

Representing excess of rent charged to departments and included in item 23, Operating Expenses, over rent paid or accrued.

TELEPHONE RENTAL, representing amounts received from telephone companies in payment for space occupied by pay-stations in the store.

INTEREST CHARGED TO DEPARTMENTS and included in item 23.

DISCOUNT EARNED ON OTHER THAN MERCHANDISE PURCHASES

SALES OF BOXES, WASTE, ETC.

INTEREST ON RECEIVABLES

*For internal operating purposes, or for comparisons with past operations, where the merchant desires to obtain the equivalent of that which is sometimes termed "Gross Profit", a figure comparable to this may be obtained by subtracting item No. 20 from item No. 7, which may be called "Gross Income from Merchandising".

INTEREST ON SECURITIES—GOVERNMENT

INTEREST ON SECURITIES—OTHER

DIVIDENDS FROM INVESTMENTS

MISCELLANEOUS

OTHER LOSSES (30)

This item represents non-operating losses.

OTHER INCOME OR LOSSES—NET (31)

This item is **Other Income** less **Other Losses.**

NET PROFIT OR LOSS (32)

This item is **Operating Profit or Loss** plus or less **Other Income or Losses—Net.**

PROVISION FOR FEDERAL INCOME TAXES (33)

These taxes are not an expense but rather a sharing of profits with the government. This item therefore represents that proportion of item 32, Net Profit which will satisfy the requirements of the government as specified in the tax laws applicable to the period.

BALANCE TO CURRENT PROFIT AND LOSS (34)

This item is **Net Profit or Loss** less **Provision for Federal Income Tax** and represents the net accretion or impairment of capital for the period.

OPERATING ACCOUNTS

DEFINITIONS

STOCK TURNOVER

Stock turnover is the figure arrived at by dividing the average inventory at retail for the period under consideration into the sales for the same period, or by dividing the average inventory at cost into the cost of sales. In the interests of uniformity, it is recommended that the first, or retail method be adopted whenever the retail inventory method is used.

AVERAGE INVENTORY

The average inventory, either cost or retail, for a given period is determined by adding together the total amounts of all the inventories recorded within such period, including the initial inventory, and dividing the figure so arrived at by the number of inventories so recorded. For example: Add together the initial inventory and the inventories recorded at the end of each week during the year and divide their sum by 53; or add together the initial inventory and the inventories recorded at the end of each month and divide their sum by 13. The second method, while more practicable than the first, is not as accurate, since exceptionally high or low inventories occurring at times other than the end of a calendar month will not be included in the calculation and hence will not affect the average.

The larger the number of recorded inventories within the period the more nearly will the resultant average inventory approximate the truth and the more accurate will be the turnover arrived at by using it as a divisor.

SALE

A sale is a transaction whereby, in exchange for cash or a promise to pay either expressed or implied, title to merchandise bought by the merchant for resale at a profit or manufactured by him either in whole or in part for sale at a profit, passes to a purchaser. The definition in the Uniform Sales Act reads: "A sale of goods is an agreement whereby the seller transfers the property in goods to the buyer for a consideration called the price."

RETURNS

A return is a transaction whereby, in exchange for the physical return of and title to merchandise previously sold, the merchant refunds the purchase price to the customer or credits his account.

ALLOWANCES

An allowance is a reduction which the merchant for any reason may find it expedient to make in the price of the merchandise involved in any sale previously concluded.

CUSTOMERS' AND EMPLOYEES' DISCOUNTS

Customers' and Employees' Discounts are reductions in the price of merchandise agreed upon between buyer and seller before the conclusion of the sale and actually granted in the transaction in which title passes, becoming thereby a part of the original purchase transaction.

RETAIL INVENTORY METHOD

The retail method of taking inventory has been laid down by the government in TREASURY DECISION 3058 issued August 16, 1920, and in a letter to the National Retail Dry Goods Association relative thereto sent from the Treasury Department January 21, 1921.*

*(T. D. 3058)

INCOME TAX

Section 203, Revenue Act of 1918: Inventories of Retail Dry Goods Dealers

"TREASURY DEPARTMENT
OFFICE OF COMMISSIONER OF INTERNAL REVENUE
Washington, D. C.

TO COLLECTORS OF INTERNAL REVENUE AND OTHERS CONCERNED:

Regulations 45 are hereby amended by inserting Article 1588, reading as follows:

ARTICLE 1588. **Inventories of Retail Dry Goods Dealers.** (1) Retail dry goods dealers who employ the 'retail method,' which is essentially a 'cost' method of valuing inventories, will be permitted to make their returns upon that basis, provided (a) that the use of such method is designated upon the return, (b) that accurate accounts are kept, and (c) that such method be adhered to in subsequent years, unless a change is authorized by the Commissioner. The 'retail method' consists in computing the 'cost' of goods on hand from the 'percentage of purchase mark-up' and the 'retail value' of goods on hand.

(2) A taxpayer employing the 'retail method' of valuing inventories shall maintain and preserve in permanent form, for the inspection of internal revenue officers, the accounts and records of each year, together with a schedule of all mark-downs in each department, and such mark-downs shall not be included in the computation of the retail value of goods on hand unless the goods so marked down have been actually sold.

(3) The following general plan of taking an inventory by the 'retail method' will, it is believed, be found readily adaptable to the requirements of most retail dry goods dealers:

(A) **The percentage of purchase mark-up** is computed as follows: The value of all merchandise, as received, is recorded by departments at two prices, (a) invoice cost plus transportation, and (b) original retail sale price. These cost and retail values are accumulated as recorded during the year. The total retail value minus the total cost value equals the total purchase mark-up, which divided by the total retail value gives the percentage of purchase mark-up.

(B) **The retail value of goods on hand** is computed as follows: A record is kept of (a) the amounts of all sales at retail, (b) any variations from the inventory prices of the preceding year of goods carried over from that year, and (c) any variations from the original sale prices, such as subsequent mark-ups or mark-downs (note paragraph 2). The retail value of the opening inventories plus the retail value of the purchases (plus or minus the algebraic sum of all subsequent mark-ups, and mark-downs in the case of goods actually sold) minus the retail value of the sales equals the retail value of the book inventory of goods on hand. Physical inventories by departments are taken of goods on hand at retail at the close of the taxable year, and the retail value of the book inventory of goods on hand is adjusted accordingly.

(C) **The cost of goods on hand** is computed by subtracting from one hundred per cent, the percentage of purchase mark-up, which gives the percentage of cost, and multiplying the retail value of goods on hand by such percentage of cost.

(Signed) PAUL F. MYERS,
Acting Commissioner of Internal Revenue.

Approved: August 16, 1920.
S. P. GILBERT, JR.
Acting Secretary of the Treasury."

"TREASURY DEPARTMENT
Washington, January 21, 1921.

National Retail Dry Goods Association,
200 Fifth Avenue,
New York, N. Y.

Sirs: Reference is made to your letter of January 13, 1921, relative to Treasury Decision No. 3058, issued August 16, 1920 (Article 1588 —Inventories of Retail Dry Goods Dealers), asking for further details as to proper procedure within the meaning of the Regulations.

Your questions are taken up and answered in the order you have presented them:

1. The use of the retail method is by the decision confined to retail dry goods dealers. Other organizations and individual stores who conduct retail establishments and follow essentially the retail method of dry goods stores, may be allowed this method upon application to the Bureau of Internal Revenue.
2. **The designation of the method as a 'cost' method.** It was not intended that the apparent limitation should be inflexible. It is recognized that on a constant or rising market the retail method is approximately a 'cost' basis and that on a falling market it results in a reduction to 'cost or market, whichever is lower.'
3. **Preserving records.** There must be a permanent form of recording by departments, purchases showing the firm name, date of invoice, invoice cost, and retail sales price. A permanent record must be kept of the accumulation of all department purchases, mark-downs, sales, stocks, etc. It must be borne in mind that under no circumstances will arbitrary standard percentages of purchase mark-up be allowed in the determination of the 'cost' or 'cost or market' value of retail inventories, but that such percentage must be the purchase mark-up percentage disclosed by the department records of the fiscal period for which the return is made.
4. **Opening Inventory.** In section 'A' the words 'the value of all merchandise as received' is inclusive of inventory at the beginning of the period. The purchase mark-up must be computed as follows:

   Cost: Inventory at cost at beginning
   Purchases at cost
   Transportation

   Retail: Inventory at sales price
   Purchases at sales price
5. **Appreciation in retail values of goods on hand.** Within the meaning of the Article, it is proper to include as a part of 'original retail sales price' the actual increase in the original sales price which has been brought about by market conditions or by incorrect pricing when the goods were put into stock.

   For the convenience of the examining officer, a special form should be provided; complete information by items of the increased form the original retail must be shown; reference, if possible, must be made to the original invoice; entry and the reason for the increase freely explained. All such amended retail increases must be approved by the buyer of the department and merchandise manager or other responsible official and they should be so filed that quick reference to them may be made. Entry of such increased retail properly belongs in department purchase books, although it may be set up as a separate item in the accumulated records of the department. The same forms that are used to record such price increases should not be used for mark-downs and in no instance will a store be allowed to include as retail increases a mark-up which has been taken as a correction or cancellation of a mark-down; such mark-up must be regarded and treated in all cases as opposite to mark-down.
6. **Proper mark-downs substantiated by record of facts will be permitted.** The decision is not intended to disturb the procedure in stores which have properly handled mark-downs, but instances where arbitrary reductions from retail values have been made because of the desire to provide for depreciation and obsolescence with no actual offering to the public of the goods on which the mark-downs were claimed, cannot be recognized. Under no circumstances will a store be allowed to depreciate its stock in any way except by the offering of it to its customers at such reduced prices. The procedure of stores in regard to mark-downs will be deemed proper if in any fiscal year or period of that year the goods so marked down are in proportion to current sales, to stock on hand, to mark-down of preceding months of preceding year, or if evidence can be submitted as to market changes which have forced a reduction in retail prices necessary to bring about a parity with the selling price of the same goods which have been purchased or could be purchased at a reduced cost.

In conclusion it should be noted that a store who has employed its retail method in the past, may now specify in the return that such method is used, as a basis on valuing inventories, regardless of the fact that in past years it reported on a 'cost' or 'cost or market whichever is lower' basis. However, the use of the retail method will not be recognized unless it has been correctly followed throughout the entire fiscal or calendar year period for which the return is made.

Respectfully,
(Signed) WM. M. WILLIAMS
Commissioner."

The Government's requirements are met by the following formula:

RETAIL INVENTORY METHOD

FORMULA

	(1) Cost	(2) Retail	(3) Mark-up	(4) % of Mark-up
1 Opening Inventory (lines 9 and 10 of preceding period).	.... ..	.... ..	.... ..	.... ..
2 Purchases..........	.... ..	.... ..	.... ..	.... ..
3 Freight Express and Cartage, Inward..........	.... ..	xxx xx	xxx xx	xxx xx
4 Additional Mark-Ups, less additional Mark-Up Cancellations..........	xxx xx	.... ..	xxx xx	xxx xx
5 Total of Inventory, plus Additions..........	.... ..	.... ..	.... ..	.... ..
6 Net Sales..........	xxx xx	.... ..	xxx xx	xxx xx
7 Mark-Downs, less Mark-Down Cancellations..........	xxx xx	.... ..	xxx xx	xxx xx
8 Total Retail Deduction (sum of items 6 and 7)........	xxx xx	.... ..	xxx xx	xxx xx
9 Resultant Retail Inventory (Retail Inventory on line 5, Column 2, minus item 8)..........	xxx xx	.... ..	xxx xx	xxx xx
10 Calculation of Cost Percentage:				
(a) Total Percentage.......... 100%				
(b) Percentage of Mark-Up (line 5, Col. 4).... ...%				
(c) Percentage of Cost [(a) minus (b)]. ....%				
11 Cost Inventory (item 10 (c) applied to item 9)..........	.... ..	xxx xx	xxx xx	xxx xx
12 Resultant Mark-Up and Percentage (item 9, minus item 11)..........	xxx xx	xxx xx	.... ..	.... ..
13 Gross Cost of Merchandise Sold (difference between Cost Inventories on lines 5 and 11)..........	.... ..	xxx xx	xxx xx	xxx xx

OPERATING ACCOUNTS

CUSTOMS AND USAGES

In the descriptive text accompanying item 15 on the operating statement, it is stated that some businesses treat their cash discounts on merchandise purchases as a reduction of the cost of those purchases, while others consider them as "Other Income" and credit them as such at the bottom of the operating statement after Net Operating Profit (or Loss) is determined.

Business men who use the first method support it by citing, first, its admitted soundness from the standpoint of accounting theory, and, second, its advisability from the merchandising standpoint by reason of the fact that the crediting to departments of everything that they earn constitutes the most effective incentive for department managers, particularly where they operate under some bonus or profit-sharing method. They say that the best way to make a merchant out of a department manager is to cause him to operate with a **complete** instead of only a **partial** knowledge of the facts.

On the other hand, those who consider discounts as "Other Income," while they show no disposition to question the accounting correctness of the other method, do challenge its expediency in no uncertain way. They advance the argument that discounts are the store's "anchor to windward," safe-guarding it as a business entity against the merchandising mistakes of department managers whose abilities vary widely both as between individuals and as between different years in the same individual's career. This argument, of course, applies increasingly with the size of the business and the degree of departmentization within it. Moreover, they quote many of the most prominent merchants of the country to the effect that their success has been built on the careful reservation of their cash discounts.

Their opponents grant that, in so far as mark-up is concerned, the retail price of the merchandise should be determined without deducting the discount from the invoice cost, but claim that the admitted advisability of this does not vitiate their other arguments.

Whatever the numerical strength of the opposing factions on this question, the fact remains that there is a decided division of opinion which necessitates the accounting treatment of this item as shown on the Operating Statement. The location of item 15 permits of either application.

PART III

CLASSIFICATION AND DISTRIBUTION OF EXPENSE

DESCRIPTIVE TEXT

The Classification and Distribution of Expense is one of the important, if not the most important, items entering into the accounting of retail stores, and unless properly handled, may vitally affect the net results of a department or business.

Operating conditions in localities and individual stores vary greatly; therefore, in order to provide methods that would be generally adaptable, there must be flexibility. In this publication, therefore, the expenses have been minutely subdivided as to selling, service, manufacturing and alteration departments.

This expense classification has been compiled for the smaller store which desires a simple, practical distribution of expense, as well as for the larger store which requires a detailed distribution of expense. The small and large classifications have been so arranged as to dovetail into each other.

The expense classification has been so drafted that it is possible for any store, regardless of size, to accomplish any or all detail desired. As the purpose of the small stores first accounting procedure is the result of the business as a whole, so we have used this as the basis of the expense classification and gradually expanding until the classification is completely departmentized. Departmental classification of expenses is the outgrowth of a classification that pertained to the business as a whole, without regard for departments.

FACTORS

The two principal factors of expense classification and distribution are as follows.

FIRST FOURTEEN (14) NATURAL DIVISIONS
SECOND FIVE (5) FUNCTIONAL GROUP CLASSIFICATIONS

The Natural Divisions of Expense are those divisions or accounts to which expense is naturally classified or charged.

The Functional Group Classifications of Expense represents the grouping of the Natural Divisions as they may apply to the functional operations of a store.

These factors are referred to in the above order, as in charging or classifying an item of expense the Natural Division is usually first determined or known, before it is classified as to which function of the store it may apply.

It is essential that stores should be departmentized, and in classifying and distributing an item of expense, the Natural Division determines the class of expense and is only a factor in departmental expenses in so far as maintaining detail analysis is concerned.

NATURAL DIVISIONS

The Fourteen (14) Divisions of Expense are natural or major divisions into which all items of expense normally fall and are as follows:

01 SALARIES AND WAGES
02 RENTALS
03 ADVERTISING
04 TAXES
05 INTEREST
06 SUPPLIES

07 SERVICE PURCHASED
08 UNCLASSIFIED
09 TRAVELING
10 COMMUNICATION
11 REPAIRS
12 INSURANCE
13 DEPRECIATION
14 PROFESSIONAL SERVICES

The Fourteen (14) Divisions are arranged in order of their relation to a business from the viewpoint of the volume of expenditure and are the basic accounts for distribution of expenses. These accounts afford a simple classification of expense for the small store which can be expanded to suit the volume of business of the individual merchant or his own desire for detailed analysis.

The numbers shown opposite each of the divisions are the basic numbers used in the numbering plan herein employed.

The major items of expense, properly chargeable to the respective captions of the Fourteen (14) Natural Divisions, are summarized as follows:

SALARIES AND WAGES (01)

Salaries and Wages include all compensation to employees for salaries, wages, commissions, bonuses, P. M.'s and suppers.

RENTALS (02)

Rentals include all rents paid for premises occupied and interest on valuation of owned premises, or if premises are leased and the business has made improvements, both rents paid and interest on investment therein should be considered as rental. The rate of interest on owned premises should be based upon six percent (6%) for the purpose of comparison. Taxes and Insurance should be charged to their respective accounts when premises are leased, subject to the payment of these items, or when they are owned.

The charts of expense accounts provide for the charging of rents to selling, alteration and manufacturing departments, windows and to garage if you maintain your own delivery equipment, for the purpose of simplicity. Rents for outside buying offices should be accordingly charged.

If any of the premises owned or leased are rented, the income and expense should be handled as a separate operating unit and not under this caption.

ADVERTISING (03)

Advertising includes all newspaper, periodical and program space, street-car cards, billboards, catalogs, circulars, electric signs, novelties and contributions that have a direct advertising value.

TAXES (04)

Taxes include all city, county and state taxes on land, buildings, fixtures and equipment and merchandise, moneys, accounts, etc., state excise or corporation, federal capital stock, state taxes of outside buying offices and licenses.

INTEREST (05)

Interest is included on the net investment in the business, except that on owned land and buildings or the improvements on leased premises which has been provided for under rent.

The interest on merchandise should be computed on the average cost inventory at the end of the period; fixtures and equipment on the depreciated value at the beginning of the period; on all other assets used in the regular operation of the business, including cash, customers and employees' notes and accounts, merchandise in transit and paid for in advance, deferred charges and any other operating assets, less liabilities and reserves, but excluding capital stock, investment accounts of owners, and profit and loss or surplus.

Liabilities having been deducted in computing net assets, the interest on borrowed capital, either notes or accounts should be included under this caption. All interest earned on notes or accounts in the regular course of business should be credited to interest on notes and accounts referred to in the preceding paragraph.

Interest earned on investments outside of the regular operations of the business should not be included under this caption.

The interest computations should be based upon six percent (6%) for the purpose of uniformity and comparison.

SUPPLIES (06)

This division includes all supplies used in operating the business, including all items classed as supplies and water, coal, gas and publication subscriptions.

SERVICE PURCHASED (07)

This division is provided to take care of light, heat and power and delivery, only when this class of service is purchased from outside sources.

UNCLASSIFIED (08)

Divisions not definitely provided for under other captions are herein included and comprise classified advertising, memberships and dues, entertainment, welfare, inspection fees, carfare, cashiers' shortages, errors, donations (cash), unauthorized purchases, discount not taken or not allowed, etc.

TRAVELING (09)

Traveling expenses incurred in connection with operating the business, including buying and selling.

COMMUNICATION (10)

This division includes all postage, (except parcel postage on packages,) telephone, telegrams and cable charges.

REPAIRS (11)

Repairs to buildings, fixtures, equipment, power plant and delivery equipment should be included in this account and consists of all ordinary repairs to buildings and equipment, for which depreciation has not been provided for. New equipment or improvements that are proper charges to capital assets should not be herein included.

INSURANCE (12)

This division includes all forms of insurance covering losses sustained from fire, liability, sprinkler leakage, use and occupancy, life and theft.

DEPRECIATION (13)

Depreciation includes the amount considered as covering amortization, wear, tear and obsolescence of buildings, leasehold, fixtures and equipment. Under this caption is also included losses resulting from, or reserve provided for bad accounts.

PROFESSIONAL SERVICES (14)

This division includes all legal, accounting, secret service and advertising professional services purchased, credit information and collection costs.

The dual numbering system has been adopted, as it affords an expansion to ninety-nine (99) subdivisions for each division if desired.

The subdivisions of each Natural Division are shown by Chart 16, Volume II, in numerical order, divided into three (3) classes of stores, so as to provide for the small and the large store. This chart will assist the small store in the allocation of items of expense to the proper account and furnishes the relation of accounts of the different classes of stores, one to another.

It is suggested that the numbering plan herein used be adopted; expanding when necessary, or using such subdivisions as meet the individual conditions, as this will place all stores, large or small, on a standardized basis and work for uniformity. The basis of successful standardization in accounting in other classes of business has been the general adoption of a fixed numbering plan by which the accountant becomes as familiar with the number as with the name of the account.

Where a complete numbering system is already in operation or where in a small business a more simple system is preferred, the store's own numbering plan may be continued, provided, that whenever reports or figures are prepared for comparison with other stores, reference is made in such reports to the standard numbers as required in this classification. In this connection Charts 16 and 17 have been prepared, so that a store may place their own account number opposite the respective division or subdivision.

FUNCTIONAL GROUP CLASSIFICATIONS

The Five (5) Group Classifications of Expense follow closely the natural functions of a store, as follows:

A ADMINISTRATIVE
O OCCUPANCY (including LIGHT, HEAT AND POWER)
P PUBLICITY
B BUYING
S SELLING (including DELIVERY)

The Five (5) Group Classifications are arranged in sequence of the usual organization procedure.

The letters shown opposite each functional group are the designated symbols for each group classification and should be prefixed to all items of expense charged direct to selling departments.

In alloting numbers and letters throughout the entire expense classification it has been the purpose to avoid duplications and have each symbol represent an individual item, grouping or designation without confliction.

ADMINISTRATIVE (A)

This function covers all of the General Administrative Expenses of a store and includes Executive Offices, Accounting Offices, Credit Offices, Superintendency and General Store Expenses.

OCCUPANCY (O)

Items applicable to maintaining the premises occupied, including fixtures and equipment, have been grouped under the Occupancy function and include rentals of buildings or interest on owned premises, taxes, insurance, depreciation, light, heat and power, and cost of maintaining all buildings and fixtures, so that they may be used for retail purposes.

PUBLICITY (P)

Under this function is included all items pertaining to newspaper, circular, bill board and other forms of advertising, interior, exterior and window displays.

BUYING (B)

Included under this function are all items pertaining to the buying of merchandise and includes merchandising offices, outside buying offices, merchandise comparison office, receiving, marking and stock rooms.

SELLING (S)

This function covers all of the expenses necessary in the selling of the merchandise from the time it is received in the department up to and including the cost of delivery to the customer and including any adjustments made thereafter.

This grouping of expense expenditures is in accordance with the operating functions of a retail store and affords easy comparison and effective control.

Merchants will find these functional groupings especially suited to any retail store, regardless of size, and as the small store develops, or greater detail is desired, the respective groups can be expanded into their subdivisions.

The subdivisions or departments into which the Five (5) Group Classifications may be respectively subdivided, classified as to four (4) classes or sizes of stores, are shown on Chart 9 and allow for flexibility between the classes to meet individual operating conditions. The numbers shown opposite the departments applicable to the Five (5) Group Classifications are suggestive only.

All selling, manufacturing, alteration and service departments should be numbered from 1 up, in groups according to classes, allowing sufficient numbers for future expansion. The numbers allotted to each department, when prefixed to the expense division or subdivision number, will serve to identify the expense item with its exact location in the expense classification. In charging direct expenses to selling departments, the letter designating the group classification should be prefixed, so as to properly collate all items under the Five (5) Functional Group Classifications without redistribution.

ALTERATION AND MANUFACTURING

The Alteration and Manufacturing Department expenses should be distributed in accordance with the Fourteen (14) Natural Divisions, but are not applicable to the Five (5) Functional Group Classifications.

A distinction should be drawn between Alteration and Manufacturing Departments. Alteration Departments are those where the operation is (in effect) merely the completion of a sale; Manufacturing Departments are those in which either material or labor, or both, are added to the value of the merchandise, or are used in the creation of new merchandise. The Alteration Departments are chargeable to "Cost of Sales" and the Manufacturing Departments to "Inventory" through the Purchase or Transfer Account.

The letter "W" has been designated for this group of departments.

DISTRIBUTION AND PRORATION

All expenses should be charged direct, wherever possible, to the selling departments to which they apply, keeping in mind that the Five (5) Functional Group Classifications should be preserved.

The Natural Divisions and Functional Group Classifications of Expense are consolidated so as to obtain a departmental distribution, as well as detail analysis, and in this connection Charts 10, 11, 12, 13, 14 and 15, Volume II, have been prepared to exhibit the complete Chart of Expense Accounts, as they apply to each subdivision or department of the respective group classification. In connection with the charts above referred to, Chart 17, Volume II, Alphabetical Classification of Expense Accounts, will afford a ready reference for the distribution of expense items.

All expenses are chargeable either, to operating or selling departments, or to service or non-selling departments. Charges to service or non-selling departments are then redistributed to the operating or selling departments on either a cost or a prorated basis. For example, should the Circular Advertising (Publicity) Department prepare advertising matter specifically for the Millinery Department, the total cost of that circular should be ascertained and accordingly charged to the Millinery Department, thus eliminating this cost from the total operating expense of the Circular Advertising Department.

Chart 18 has been compiled so as to cover distribution of all direct and prorated expenses by classes of stores, providing simple bases of proration for the small store and more elaborate proration for those stores that desire intricate detail.

The following examples of classification of department expenses show the application and method of the numbering plan herein used.

B 409-2

B	Buying (Group Classification)
4	Millinery (Selling Department)
09	Traveling (Natural Division)
2	Traveling—Buying (Subdivision)

2406-7

24	Operating (Occupancy-Service Department)
06	Supplies (Natural Division)
7	Supplies—Operating (Subdivision)

6211-7

62	Garage and Automobiles (Selling-Service Department)
11	Repairs (Natural Division)
7	Repairs—Automobiles (Subdivision)

In connection with the distribution applicable to the small store, where the Fourteen (14) Natural Divisions are used only, the Functional Group Classifications or subdivisions do not apply, and the application is very simple; in the case of Class "A" Stores, the operation is practically the same as the examples shown, with the exception that there are virtually no subdivisions of the natural divisions.

CHARTS

In presenting the expense classification, the plan of charts, as shown in detail in Volume II, were decided as being the most complete and comprehensive form, as each chart places before the eye all detail pertaining to the respective unit of the entire plan.

The purposes of the respective charts are as follows:

CHART No. 7. Comparative Statement of Expenses. This statement is to show the detail of expenses of a business as a whole, by the Fourteen (14) Natural Divisions and the Five (5) Functional Group Classifications, for the current month and year to date, with the previous year comparisons. Separate statements should be used for owned and leased departments.

CHART No. 8. Chart of the Natural Divisions of Expense as they appear in the Five (5) Functional Group Classifications. This chart is to show which of the natural divisions are applicable to the group classifications.

CHART No. 9. Chart of Functional Group Classifications of Expense and Subdivisions thereof. This chart is to show the subdivisions or departments which apply to each group classification. This chart provides for four (4) classes of stores, and a merchant can decide which class could best be adapted to his business. It is not necessary to use each class in its entirety, but any part of one class may be used with the other class according to the desire for detail.

CHARTS Nos. 10, 11, 12, 13 and 14. Chart of Expense Accounts. These charts set forth the natural divisions of expense as they apply to each subdivision of the functional groups. There is a chart for each group.

Three (3) classes of stores have been provided on these charts, and a merchant can select the accounts best adaptable to his business.

A store that desires departmental results will be able to compile their complete chart of accounts from these charts.

Class "D" stores have not been provided for on these charts, as a store that desires this detail can compile the desired accounts from the Class "C" classification.

CHART No. 15. Chart of Expenses ordinarily chargeable direct to Selling Departments. This chart shows the accounts which apply to items that should be charged direct to selling departments and is subsidiary to Charts 10, 11, 12, 13 and 14.

In charging expenses direct to selling departments the letters A, O, P, B and S should be prefixed to the department number so that the five (5) functional groups of expenses may be maintained.

CHART No. 16. Numerical Classification of the Natural Divisions of Expense. This chart shows in numerical form the Fourteen (14) Natural Divisions of Expense and their subdivisions, classified into three (3) classes of stores and so arranged that whenever greater detail is desired the accounts in use can be referred to under the respective class of store and the expansion in the classification can be readily made, as the account numbers in each class of stores are shown opposite each other.

CHART No. 17. Alphabetical Classification of Expense Accounts. This chart or index affords an alphabetical reference to charts 10, 11, 12, 13, 14 and 15 and includes all items of expense which may or may not be directly mentioned in the Charts of Expense Accounts.

This chart should be very helpful in distributing expenses, when the account to which it may be applicable is in question.

CHART No. 18. Distribution and Proration of Indirect Expenses. This chart is provided to show the bases of proration to the selling departments of the expenses of the service departments.

Four (4) classes of stores have been provided, but if in compiling your chart of expense accounts you have taken accounts from more than one class of stores, you should follow the same plan in selecting your bases for proration of indirect expenses.

CHART No. 19. Alteration and Manufacturing "W" Division. The expense accounts of the Alteration and Manufacturing departments are shown by this chart.

CHART No. 22. Source of Information for Expense Distribution. This chart is prepared so as to convey the bookkeeping procedure, in connection with recording of expenses, in accordance with the plan outlined herein.

FLOOR SPACE RENTALS

The importance of establishing a satisfactory degree of comparison in operating costs of stores, and the relatively high proportion of such costs appearing under the caption of OCCUPANCY suggest the desired method of treating particularly upon the largest item placed under the latter heading; namely, that of RENTALS.

A clear statement of the principle of rentals in relation to standardized accounting for retail stores will serve as a guide in its application. The amount charged to RENTALS should represent the amount paid as rent for the properties used in the conduct of the business, or the occupancy value of such properties; the latter on the theory that real estate profits are quite distinct from merchandising profits. Only by the inclusion in the expenses of a merchandising business of rentals on owned properties used in that business can the merchant determine the amount of profits arising out of merchandising operations.

It is suggested that consideration be given to the following:

FIRST. The rental value of similar properties in the immediate vicinity.

SECOND. A proper return upon the apparent real estate value of the properties.

In cases wherein there is a difference between the values disclosed by 1 and 2 as above, it would in most cases be proper to establish a figure compromising between the two, for the following reasons:

> May represent a temporary condition due to extreme business conditions or to unusual leasing conditions in the vicinity, and therefore would not in itself be suitable for a basis, or may disclose an amount at variance with the leasing conditions in the immediate vicinity.
>
> There are, generally speaking, three classes of operators as follows:
>
> A. Those leasing all properties used.
>
> B. Those owning all properties used.
>
> C. Those leasing part and owning part.

Only classes B and C, as above, present any problem in determining the total rentals, and these only in the matter of the properties which are owned.

In some extreme conditions the amount paid under a lease may fail to represent an amount even approximating the value of the premises. In such cases, if the variation be of sufficient amount to justify the procedure, a value may be arrived at as in the case of owned properties, and the amount of the excess credited to a special lease account appearing under "Other Income" on the Operating Statement.

After deciding upon the amount to be charged to RENTALS for all properties used, the next process should be to determine the relative values of different parts of the properties. In this connection, consideration should be given to the following:

A. Value of the Show Windows.

B. Value of the Street Floor.

C. Value of the Basements and Upper Floors.

D. Relative values of most favorable locations.

(A) The floor space valuation of the show windows should be determined by its display value, but only in proportion to the location valuation placed on the entire street floor.

The floor space rental established is charged to Rentals 02–1 under the Window Department in the Publicity group.

(B) The value of the street floor is affected by the following considerations:

1. Exposure or frontage.
2. Number and locations of entrances.
3. Number of stories.
4. Layout of ground plan.
5. Number and location of elevators.

(C) The values of basements and upper floors are more readily determinable after the windows and street floor have been assigned a value. Basements suitable for and used as merchandising space should be accorded a higher value than if used for non-selling purposes. Usually the floors decrease in value according to their height above the ground. In this matter the adequacy of the elevator service is of prime consideration.

Generally speaking, the assignment of values inside the store building are arbitrary, but a fair disposition of the matter may be made if due consideration be given to all of the factors. The particular departments carried bear on the subject, inasmuch as certain departments are more favorably located above the street floor.

(D) It is considered fair and proper in many well regulated stores to recognize the value of certain parts of floors with a higher rental charge than other spaces not so favorably situated. These zones of higher value are usually easily located, and the matter of fixing the amount of variation should not be difficult. Departments located on important aisles or in places where customers congregate, and spaces close to elevators are examples.

Argument is made that a store may be laid out so that all departments may be assigned locations equally desirable, provided that in the plans proper consideration be given to the relation of departments to one another. It is held that in every store there is an ideal location for each department, and that no effort should be spared in determining and assigning these locations. The proponents of this theory claim that there should be no difference recognized in rental value of space used in selling, but that all area used in selling should be charged at the same rate.

As rental is to be charged to selling, alteration, manufacturing and window departments only, it is advisable to establish a per square foot rental on the various locations and floors, excluding windows, as this has been previously determined, and after measuring the spaces occupied by the selling, alteration and manufacturing departments, the rental applicable to each can be readily computed. In establishing the per square foot rental charge it should be remembered that in eliminating the service departments, the rentals of the space occupied by the other class of departments must be increased.

The application of the foregoing is more simple than may appear; in fact, the time necessary to complete all of the calculations and measurements is found to be remarkably little even in stores of larger size. For purposes of correct comparability the rental question is worthy of the particular attention directed to it.

For the guidance of those who have heretofore charged rentals upon some purely arbitrary basis, such as sales, attention is called to the necessity under this plan of providing for the recording and adjustment of departmental changes whenever they occur.

WINDOW RENTAL

The expenses in connection with the window display department, which include all operating expenses, inclusive of floor space rent, as shown by Chart 12, are chargeable to the selling departments on the basis of arbitrary values of each window or case, according to display value.

The arbitrary values of each window or case should be based upon the display value of one to another, and for example consider a store that has five windows, the best of which is arbitrarily valued at $5.00 per day and the others based upon their display value, as compared to the $5.00 per day window, are valued at two at $4.00 and two at $2.00 per day. The windows were used by selling departments during the entire thirty days of the month as follows:

Department No.	Window No.	No. of Days	Rate Per Day	Total
4	1	10	$5.00	$50.00
8	1	8	5.00	40.00
3	1	4	5.00	20.00
1	1	8	5.00	40.00
7	2	12	4.00	48.00
5	2	9	4.00	36.00
1	2	9	4.00	36.00

10	3	8	4.00	32.00
9	3	22	4.00	88.00
6	4	10	2.00	20.00
4	4	12	2.00	24.00
2	4	8	2.00	16.00
8	5	20	2.00	40.00
5	5	10	2.00	20.00
Total		150		$510.00

On the above basis the total arbitrary value charged to selling departments amounted to $510.00, which is equivalent to 100%, and accordingly proportioned to selling departments as follows:

Department No.	Arbitrary Value	Percent
1	$76.00	14.90%
2	16.00	3.14%
3	20.00	3.92%
4	74.00	14.51%
5	56.00	10.98%
6	20.00	3.92%
7	48.00	9.41%
8	80.00	15.69%
9	88.00	17.26%
10	32.00	6.27%
	$510.00	100.00%

The percentages opposite each department designate the portion of time that they used the window space, based upon the arbitrary display values of the windows to each other. The percentage having been determined, the next procedure is to distribute the total expenses of the window department to the selling departments, and the following example is offered, considering that the total expense actually incurred amounted to $400.00.

Department No.	Percent Used	Total
1	14.90%	$59.60
2	3.14%	12.56
3	3.92%	15.68
4	14.51%	58.04
5	10.98%	43.92
6	3.92%	15.68
7	9.41%	37.64
8	15.69%	62.76
9	17.26%	69.04
10	6.27%	25 08
	100.00%	$400.00

If the window rentals are handled in accordance with the above plan, no loss or profit will accrue to the business, as the actual expenses incurred will be charged to the selling departments.

ALTERATION AND MANUFACTURING DEPARTMENTS

In the operation of these departments, in accordance with the plan suggested herein, which provides that they operate on an actual cost basis and that no profit or loss accrue to them, the following procedure is suggested:

ALTERATION DEPARTMENTS

In the case where these departments work exclusive for one selling department the procedure is simple, as all expenses actually incurred are charged to Alteration Costs under the caption "Cost of Sales" of the respective selling department, in the departmental record, and in the general ledger to one account comprising all departments.

Where an alteration department does work for more than one selling department it is necessary to maintain a cost record, either actual costs as near as same can be determined, or estimated costs, which can be established for a period on each class or kind of alterations. Records should be kept by the alteration departments covering the work done for each selling department, based upon the cost of each alteration made and the total amount applicable to each selling department computed in percentage, as its ratio in percent bears to the grand total of all costs completed during the period by the alteration department.

The total of the expenses of the alteration department can be transferred to the respective selling departments, apportioned on the basis of the percentages.

The inventory of material and supplies should be taken at the end of each month or period, if the actual expenses are desired.

The charges made to customers for alterations, which are termed "Alteration Sales," are to be included in the selling department's sales (but are to be excluded in computing the retail inventory of the selling department), as the selling department will be charged with all alterations made and is therefore entitled to the income from this source.

MANUFACTURING DEPARTMENTS

The manufacturing departments should be operated on a cost to manufacture basis. In order to accurately determine the results of manufacturing it is necessary to devise a cost system, so that all completed product manufactured can be transferred to the selling departments, either retail or jobbing, at cost; in transferring to retail selling departments, if you are on the retail method, the transfers can be retailed the same as purchases made through outside sources.

All expenses in connection with the manufacturing departments should be charged to their inventory, as all costs, as computed, should include material, labor and overhead expense.

An inventory of all material, supplies, work in process and completed product, not transferred, should be taken periodically, and the difference determined between actual and book inventories adjusted by transfer to the selling departments, that received their product during the period. The accuracy of the cost records, which are a basis of your selling price, can be ascertained.

In compiling this report no provision has been made for forms in connection with the books themselves or departmental records, as this was considered a separate task for later procedure.

PART IV

CLASSIFICATION OF MERCHANDISE

The application of the Standardization plan to merchandise classification follows in a general way the principles of the expense plan.

While differences in physical layout and personnel organization occasion somewhat varying merchandise groupings in different stores, there are, nevertheless, certain natural tendencies in the development of a logical merchandise classification. These tendencies have been followed as closely as possible in the plan.

Comparison between store merchandise operations by departments requires that there shall be similar departmental grouping of merchandise. Without this the final results when compared may disclose differences which, while they appear to be brought about by merchandise policies and methods, may be largely due to varying tendencies introduced by dissimilar groupings.

The accompanying merchandise classification chart presents the schedules as they may be adopted according to existing requirements and future developement of the individual store. It provides for the trade a standard plan which, when adopted, together with the expense classification, will bring about final profit and loss figures by departments which will serve as a satisfactory basis for comparison of operations.

It is not intended that the schedules of either merchandise or expense need be selected with regard to each other. For example, a store desiring a larger departmental classification of merchandise need not change the existing expense classification unless this is desired. The general principles of standardization are served if consistency is observed in the adoption of either merchandise or expense as a unit of the plan.

PART V

BALANCE SHEET ACCOUNTS

BOOKKEEPING PROCEDURE

The explanatory detail appearing under this caption is to assist the bookkeeper in making the book entries. It is advisable to have the general ledger divided in a manner so that the financial statements can be readily prepared from the Trial Balance. Chart number twenty-one included in Volume II will assist you in devising your general ledger, as well as furnish information as to the source of entries and the ultimate results.

ASSETS

Cash on Hand

DEBIT WITH:

(1)—Total amount of cash received.

CREDIT WITH:

(1)—Total amount of cash deposited.

Balance—Represents the undeposited cash on hand.

Cashiers' Funds

DEBIT WITH:

(1)—Amount of fund created to meet currency disbursements.

(2)—Increases in the fund originally created.

CREDIT WITH:

(1)—If the fund be decreased, credit this account with the amount by which it is diminished.

Balance—Represents the amount of the fund which is set aside to meet currency disbursements and supply store cashiers.

Cash on Deposit

DEBIT WITH:

(1)—Total amount of cash deposited.

(2)—Collections made by the bank.

(3)—Interest earned on bank balances.

CREDIT WITH:

(1)—Total amount of checks issued.

(2)—Exchange and other collection charges made by the bank.

(3)—Other proper bank charges.

Balance—Represents the available balance in the banks.

Notes Receivable

DEBIT WITH:

(1)—Face value of notes received of customers in the usual course of business.

CREDIT WITH:

(1)—Face value of notes of customers paid, discounted or otherwise disposed of.

Balance—Represents the face value of notes on hand. (If the Notes Receivable Discounted account be used, the balance of this account, less the balance of the Notes Receivable Discounted account, will represent the notes on hand. Notes that have been proven uncollectible should be written off).

Accrued Interest

DEBIT WITH:

(1)—Amount of interest accrued on notes receivable on hand.

CREDIT WITH:

(1)—Interest received on notes receivable.

Balance—Represents the amount of interest earned on notes receivable, unpaid.

Reserve for Possible Losses on Customers' Notes

Debit with:	Credit with:
(1)—All losses sustained on account of customers' notes receivable.	(1)—Estimated amount of losses on customers' notes receivable sustained during an accounting period.

Balance—Represents the available reserve for losses.

Accounts Receivable—Charge Accounts

Debit with:	Credit with:
(1)—Total charge sales.	(1)—All moneys received from customers to apply on account, plus the discounts allowed.
(2)—Freight, expressage and parcel post chargeable to customers.	(2)—Allowances to customers for goods returned and claims allowed.
(3)—Transfers from C. O. D., Layaway and Installment accounts, when changed to open accounts.	(3)—Uncollectible accounts written off.
	(4)—Transfers to C. O. D., Layaway and Installment accounts, when changed from open accounts.

Balance—Represents the amount due and collectible from customers, and should agree with the results of trial balance compiled from the customers ledgers.

Accounts Receivable—C. O. D. Accounts

Debit with:	Credit with:
(1)—Total C. O. D. sales.	(1)—All moneys received from customers to apply on C. O. D. accounts, plus the discounts allowed.
(2)—Freight, expressage and parcel post chargeable to customers.	(2)—Allowances to customers for goods returned and claims allowed.
(3)—Transfers from Charge, Layaway and Installment accounts, when charged to C. O. D. accounts.	(3)—Uncollectible accounts written off.
	(4)—Transfers to Charge, Layaway and Installment accounts, when changed from C. O. D. accounts.

Balance—Represents the amount due from customers, and should agree with the results of a trial balance compiled from the C. O. D. ledgers.

Accounts Receivable—Will-Call or Layaway Accounts

Debit with:	Credit with:
(1)—Total Will-Call or Layaway Sales.	(1)—All moneys received from customers to apply on Will-Call, or Layaway accounts, including discounts.
(2)—Freight, expressage and parcel post chargeable to customers.	(2)—Allowances to customers for goods returned and claims allowed.
(3)—Transfers from Charge, C. O. D. and Installment accounts when transferred to Layaway accounts.	(3)—Uncollectible accounts written off.
	(4)—Transfers to Charge, C. O. D. and Installment accounts, when changed from Will-Call or Layaway accounts.

Balance—Represents the amount due from customers, and should agree with the results of a trial balance compiled from the Will-Call or Layaway ledgers.

Accounts Receivable—Installment Accounts

Debit with:

(1)—Total installment sales.

(2)—Freight, expressage and parcel post chargeable to customers.

(3)—Transfers from Charge, C. O. D., and Layaway accounts, when transferred to Installment accounts.

(4)—Interest charged on Installment accounts.

Credit with:

(1)—All moneys received from customers to apply on account, plus discounts allowed.

(2)—Allowances to customers for goods returned and claims allowed.

(3)—Uncollectible accounts written off.

(4)—Transfers to Charge, C. O. D. and Layaway or Will-Call accounts, when changed from Installment accounts.

Balance—Represents the amount due from customers, and should agree with the results of a trial balance compiled from the Installment ledgers.

Reserve for Possible Losses on Customers' Accounts

Debit with:

(1)—All losses sustained on account of customers' accounts receivable.

Credit with:

(1)—Estimated amount of losses on customers' accounts receivable sustained during accounting period.

Balance—Represents the available reserve for losses.

Merchandise on Hand—Inventory

Debit with:

(1)—Value of merchandise on hand at beginning of the period.

(2)—Cost of all merchandise received.

(3)—Freight, expressage and parcel post, including cartage, on merchandise purchases.

Credit with:

(1)—Cost of merchandise sold.

(2)—Cost of merchandise returned to vendors, and allowances made.

Balance—Represents the value of merchandise on hand at the end of the period.

Note: Divergence from this practice is noted in the fact that some accountants prefer to maintain the following separate accounts:

Inventory at the beginning of period (To remain unchanged during the period).

Purchase Account (To which Debit items No. 2 and 3, and Credit items No. 1 and 2, shown above, apply).

Manufacturing Inventory

Debit with:

(1)—Amount of Material purchased.

(2)—Amount of Labor and Expenses incurred in manufacturing.

Credit with:

(1)—Amount of Merchandise manufactured and transferred at cost to Selling Departments.

Balance—Represents amount of Material and Goods in Process not having been transferred to the Selling Departments.

Note: This forms a part of the Inventory of Merchandise on Hand account on the Balance Sheet, but to be kept separate on the ledger.

Advances on Merchandise Purchases

Debit with:

(1)—Moneys advanced on contracts for the purchase of merchandise.

Credit with:

(1)—Amount of advances on shipments made, transferring the charge to "Inventory of Merchandise on Hand" account.

Balance—Represents amount of money advanced on purchase contracts.

United States Bonds

Debit with:

(1)—Cost of bonds purchased.

Credit with:

(1)—Cost of bonds disposed of. The difference between the cost and selling price should be charged or credited to "Other Income" account.

Balance—Represents the cost of bonds on hand.

Note: If the number of transactions in U. S. Bonds be large, this account, as designed, will be entirely inadequate, for the reason that when large numbers of bonds are charged to this account at cost it becomes very difficult to reconcile the balance shown by the account with the actual count of the bonds on hand, each bond probably having been taken into the account at a different cost, while the bond bears only the par value. This complication arises also in the event of sale when it becomes necessary to determine the profit or loss on the sale. It is, therefore, recommended that each bond be entered separately, identified by serial number, and that the actual count be made according to the serial numbers of the bonds, and not the face or par value; or that the cost of each bond be written on the bond; or, preferably, that the bonds be charged and credited to this account at face value and not at cost, the difference being credited or charged to an account termed "Reserve for Discount on U. S. Bonds."

Certificates of Indebtedness

Debit with:

(1)—Cost of certificates of indebtedness purchased.

(1)—Cost of certificates of indebtedness disposed of. The difference between the cost and selling price should be charged or credited to "Other Income" account.

Balance—Represents the cost of certificates of indebtedness on hand.

Accrued Interest
U. S. Bonds and Certificates of Indebtedness

Debit with:

(1)—Amount of interest accrued on U. S. Bonds.

(2)—Amount of interest accrued on certificates of indebtedness.

Credit with:

(1)—Interest received on U. S. Bonds.

(2)—Interest received on certificates of indebtedness.

Balance—Represents the amount of interest earned but unpaid.

War Savings Stamps

Debit with:

(1)—Cost of War Saving Stamps purchased.

Credit with:

(1)—Cost of War Saving Stamps disposed of. The difference between the cost and selling price, representing interest, should be credited to "Other Income" account.

Balance—Represents the cost of War Savings Stamps on hand.

Reserve for Possible Losses on U. S. Securities

Debit with:

(1)—All losses sustained on U. S. securities.

Credit with:

(1)—Estimated amount of losses on U. S. securities sustained during the accounting period.

Balance—Represents the available reserve for losses.

Securities Owned—Other Corporations

Debit with:

(1)—Cost of securities of other corporations purchased.

Credit with:

(1)—Cost of securities of other corporations disposed of. The difference between the cost and selling price should be charged or credited to "Other Income" account.

Balance—Represents the cost of securities of other corporations on hand.

Notes Receivable—Non-Current

Debit with

(1)—Face value of notes received other than from customers.

Credit with:

(1)—Face value of non-current notes paid, discounted or otherwise disposed of. (See note above under "Notes Receivable.")

Balance—Represents the face value of non-current notes on hand.

Accrued Interest

Debit with:

(1)—Amount of interest accrued on non-current notes receivable.

Credit with:

(1)—Interest received on non-current notes receivable.

Balance—Represents the amount of interest earned but unpaid.

Insurance Deposits

Debit with:

(1)—Credits in the hands of mutual insurance agencies.

Credit with:

(1)—Withdrawal of funds.

Balance—Represents funds on deposit with mutual insurance agencies.

Cash Surrender Value of Life Insurance Policies

Debit with:

(1)—That portion of the premium paid equal to the increase in the cash surrender value of the policy as compared with the value at the time of the previous premium payment.

Credit with:

(1)—Cash received at the maturity or surrender of the policy.

Balance—Represents cash surrender value of life insurance policies.

Common Carrier Claims

(An Account with each Transportation Company)

Debit with:

(1)—Amount of claims made against common carriers for loss or damage in transportation.

Credit with:

(1)—Amount of claims cancelled or reduced.

(2)—Amount of claims paid.

Balance—Represents amount of claims due from common carriers.

Land and Buildings—Not used in Operations

DEBIT WITH:

(1)—Cost of land and buildings purchased.
(2)—Carrying charges on non-income producing lands.
(3) Cost of additions to buildings.

CREDIT WITH:

(1)—Cost value of land and buildings appropriated for operating purposes.
(2)—Amount realized from sales.

Balance—Represents value of investments in land and buildings not used in the operation of the business.

Personal Accounts—Officers, Stockholders and Employees

DEBIT WITH:

(1)—Total charges to officers, stockholders and employees.

CREDIT WITH:

(1)—All moneys received from and other credits to officers, stockholders and employees, including discounts.
(2)—Uncollectible accounts written off.

Balance—Represents the amount due, and should agree with the results of a trial balance compiled from the ledgers.

Unexpired Insurance Premiums

DEBIT WITH:

(1)—Insurance premiums paid.

CREDIT WITH:

(1)—The amount of premiums accrued.

Balance—Represents the cost of insurance unexpired.

Prepaid Interest on Notes Payable

DEBIT WITH:

(1)—Interest paid in advance.

CREDIT WITH:

(1)—Amount of interest accrued.

Balance—Represents the amount of prepaid interest on notes.

NOTE: For balance sheet purposes, include under "Prepaid Expenses."

Supply Inventory

DEBIT WITH:

(1)—Cost of supplies purchased in large quantities.

CREDIT WITH:

(1)—Cost of supplies used during the period.

Balance—Represents the cost of supplies on hand.

NOTE: Supplies purchased in small quantities should be charged directly to the appropriate expense account.

Prepaid Expenses

DEBIT WITH:

(1)—Expenditures made for expenses that may be spread over a period of time, or with any debit made for any other reason that may be amortized through charges made to expense or other income accounts at intervals over a period of time. An appropriate account to be opened with each such expenditure, loss or debit.

CREDIT WITH:

(1)—The pro-rata proportion chargeable to expense or other income account.

Balance—Represents the amount of prepaid expenses.

Organization Expenses

Debit with:	Credit with:
(1)—Cost of organizing and preparing an enterprise to do business and produce income.	(1)—Pro-rated amount for the period.

Balance—Represents the unmatured balance of organization expenses.

Land

Debit with:	Credit with:
(1)—The purchase contract price of the land. (2)—Cost of surveying, title insurance, recording fees, broker's commission, taxes owing at date of purchase. (3)—Cost of local improvement taxes and assessments. (4)—Cost of carrying charges until buildings are erected.	(1)—Cost of land sold.

Balance—Represents the cost value of land owned.

Leasehold and Improvements to Leased Buildings

Debit with:	Credit with:
(1)—Cost of leasehold. (2)—Cost of improvements to and betterments on leased buildings.	(1)—Cost of leasehold at the expiration of the lease. (2)—Cost of improvements and betterments at the expiration of the lease.

Balance—Represents the cost value of leasehold and improvements to leased buildings.

Reserve for the Amortization of Leasehold

Debit with:	Credit with:
(1)—Cost of leasehold at its expiration. (2)—Cost of improvements and betterments at the expiration of the lease.	(1)—A periodical allowance spread over the life of the lease.

Balance—Represents the reserve for amortization of leasehold and improvements to leased buildings.

Buildings

Debit with:	Credit with:
(1)—Actual cost of buildings purchased or constructed. (2)—Improvements and additions. (3)—Cost of replacing buildings, or material parts thereof, destroyed by fire, wear, tear, etc.	(1)—Cost of buildings abandoned, destroyed, replaced or sold.

Balance—Represents the cost value of buildings owned.

Note: Improvements include the enlargement or improvement of existing structures.

Additions include additional structures not taking the place of anything previously existing.

Replacement is either the re-erection of an entire structure, or the construction of some specific and material portion of it, such as a new roof.

Repairs are chargeable to "Occupancy" expense or to "Other Income."

Reserve for Depreciation of Buildings

Debit with:	Credit with:
(1)—Amount of depreciation taken on articles discarded, destroyed or sold.	(1)—A periodical allowance for depreciation.

Balance—Represents the reserve for depreciation of buildings.

Machinery and Equipment

Debit with:	Credit with:
(1)—Cost of machinery and equipment purchased, and installation thereof.	(1)—Cost of machinery and equipment discarded, destroyed or sold.
(2)—Cost of additions or alterations, provided original efficiency is thereby increased.	
(3)—Cost of replacing any article previously charged to this account.	
(4)—Improvements and additions.	

Balance—Represents cost value of machinery and equipment on hand.

Reserve for Depreciation of Machinery and Equipment

Debit with:	Credit with:
(1)—Amount of depreciation taken on articles discarded or sold.	(1)—A periodical allowance for depreciation.

Balance—Represents the reserve for depreciation of machinery and equipment.

Store Furniture and Fixtures

Debit with:	Credit with:
(1)—Cost of store furniture and fixtures purchased.	(1)—Cost of articles discarded, destroyed or sold.
(2)—Cost of replacing any article previously charged to this account.	
(3)—Improvements and additions.	

Balance—Represents the cost value of store furniture and fixtures on hand.

Reserve for Depreciation of Store Furniture and Fixtures

Debit with:	Credit with:
(1)—Amount of depreciation taken on articles discarded, destroyed or sold.	(1)—A periodical allowance for depreciation.

Balance—Represents the reserve for depreciation of store furniture and fixtures.

Office Furniture and Equipment

Debit with:	Credit with:
(1)—Cost of office furniture and equipment purchased.	(1)—Cost of articles discarded, destroyed or sold.
(2)—Cost of replacing articles previously charged to this account.	
(3)—Improvements and additions.	

Balance—Represents the cost value of office furniture and equipment on hand.

Reserve for Depreciation of Office Furniture and Equipment

Debit with:
(1)—Amount of depreciation taken on articles discarded, destroyed or sold.

Credit with:
(1)—A periodical allowance for depreciation.

Balance—Represents the reserve for depreciation of office furniture and equipment.

Delivery Equipment

Debit with:
(1)—Cost of all substantial property, direct or auxiliary, used in connection with the delivery of goods, both inward and outward.
(2)—Cost of replacing articles previously charged to this account.
(3)—Improvements and additions.

Credit with:
(1)—Cost of articles discarded, destroyed or sold.

Balance—Represents cost value of delivery equipment on hand.

Reserve for Depreciation of Delivery Equipment

Debit with:
(1)—Amount of depreciation taken on articles discarded, destroyed or sold.

Credit with:
(1)—A periodical allowance for depreciation.

Balance—Represents the reserve for depreciation of delivery equipment.

Good Will, Patents and Trademarks

Debit with:
(1)—Cost of good will, patent rights and trademarks acquired.

Credit with:
(1)—Cost of good will written off.
(2)—Cost of patent rights expiring, or a periodical allowance for amortization.
(3)—Cost of trademark becoming worthless, or a periodical allowance for amortization.

Balance—Represents the cost value of good will, patents and trademarks.

LIABILITIES

Notes Payable
For Money Borrowed from Banks

Debit with:

(1)—The face value of all notes redeemed.

Credit with:

(1)—Face value of notes issued to banks, bankers or trust companies.

Balance—Represents the face value of notes outstanding due banks.

Notes Payable
For Money Borrowed Through Brokers

Debit with:

(1)—The face value of all notes redeemed.

Credit with:

(1)—The face value of notes issued for money borrowed through brokers.

Balance—Represents the face value of notes outstanding for money borrowed through brokers.

Notes Payable
For Money Borrowed from Officers

Debit with:

(1)—The face value of all notes redeemed.

Credit with:

(1)—Face value of notes issued to officers.

Balance—Represents the face value of notes outstanding due officers.

Notes Payable
For Money Borrowed from others

Debit with:

(1)—The face value of all notes redeemed.

Credit with:

(1)—Face value of notes issued to others.

Balance—Represents the face value of notes outstanding due others.

Notes Payable
For Purchases

Debit with:

(1)—The face value of all notes redeemed.

Credit with:

(1)—Face value of notes issued to vendors.

Balance—Represents the face value of notes outstanding due vendors.

Trade Acceptances Payable

Debit with:

(1)—The face value of all trade acceptances redeemed.

Credit with:

(1)—The face value of trade acceptances given.

Balance—Represents the face value of trade acceptances outstanding.

Accounts Payable for Merchandise and Expense Purchases

Debit with:	Credit with:
(1)—Amounts allowed by vendors for goods returned and other allowances made. (2)—Freight and express chargeable to vendors. (3)—All moneys paid to vendors to apply on account, including discounts. (4)—The face value of notes and trade acceptances given vendors.	(1)—The face value of all purchase invoices.

Balance—Represents the amount owing to vendors for purchases, and should agree with the results of a trial balance compiled from the creditors' ledgers.

Accounts Payable for Federal Sales Taxes

Debit with:	Credit with:
(1)—All moneys paid to the U. S. Collector of Internal Revenue, including penalties and interest.	(1)—The amounts due as Excise Taxes. (2)—Penalties and interest assessed, if any.

Balance—Represents the amount of unpaid federal sales taxes.

Accounts Payable For Unredeemed Cash Refunds

Debit with:	Credit with:
(1)—The face value of all cash sale refund credits redeemed.	(1)—The face value of all cash sale refund credits issued to customers.

Balance—Represents the face value of cash sale refund credits outstanding.

Accounts Payable for Unredeemed Gift Certificates

Debit with:	Credit with:
(1)—The face value of all gift certificates redeemed.	(1)—The face value of all gift certificates issued.

Balance—Represents the face value of gift certificates outstanding.

Accounts Payable—Leased Section Accounts

Debit with:	Credit with:
(1)—All moneys paid lessee on account of contract. (2)—Expenses chargeable to lessee.	(1)—The amount of net profit, or percentage of net sales, due lessee per contract.

Balance—Represents the amount owing lessee.

Note: It is recommended that a separate account be kept with each lessee.

Accounts Payable—Personal Accounts

Debit with:	Credit with:
(1)—All cash withdrawal of funds on deposit or credits. (2)—Other chargeable items.	(1)—Salary credits or deposits made. (2)—Other credit items.

Balance—Represents the amount owing on personal accounts.

Accrued Taxes—Real and Personal

Debit with:
(1)—Amount of tax bills when paid.

Credit with:
(1)—Estimated proportion of taxes for the period.

Balance—Represents the amount of estimated taxes accrued, but not due.

Accrued Pay Roll

Debit with:
(1)—All moneys paid for salaries and wages.
(2)—Amounts chargeable to employees for other purposes.

Credit with:
(1)—Cost of labor and fixed salaries and wages for the period.

Balance—Represents the amount of wages accrued, but not due.

Accrued Interest on Notes Payable

Debit with:
(1)—The amount of interest paid.

Credit with:
(1)—The amount of interest accrued for the period.

Balance—Represents the amount of interest accrued, but not due.

Accrued Rent

Debit with:
(1)—Amount of rent when paid.

Credit with:
(1)—A periodical proportion of rent accrued.

Balance—Represents the amount of rent accrued, but not due.

Accrued Expenses

Debit with:
(1)—All moneys paid on account of such expenses, including discounts.
(2)—Allowances and other deductions from such expenses.

Credit with:
(1)—Amount of unpaid expenses at close of accounting period.

Balance—Represents the amount of expenses accrued, but not due.

Funded Indebtedness—Mortgages

Debit with:
(1)—Payments on account of the principal.

Credit with:
(1)—The principal sum of each mortgage given.

Balance—Represents the amount owing on account of the principal of mortgages given.

Funded Indebtedness—Bonds

Debit with:
(1)—The amount of bonds retired.

Credit with:
(1)—The amount of bonds issued.

Balance—Represents the amount of bonds outstanding.

Reserved for Federal Income Taxes

Debit with:	Credit with:
(1)—Amount of Federal Income Taxes reserved in excess of actual amount payable, if any. (2)—All moneys disbursed in payment of Federal Income Taxes.	(1)—The estimated amount of Federal Income Taxes accrued at the close of each accounting period. (2)—Amount of Federal Income Taxes payable in excess of actual amount reserved for, if any.

Balance—Represents the amount of Federal Income Taxes payable.

Reserve for Contingencies

Debit with:	Credit with:
(1)—All losses sustained on account of contingencies not otherwise provided for.	(1)—An estimated amount to cover contingent losses.

Balance—Represents the available reserve for contingencies.

Preferred Capital Stock-Authorized

Debit with:	Credit with:
(1)—Par value of preferred shares retired.	(1)—Par value of preferred shares authorized.

Balance—Represents the par value of shares authorized.

Preferred Capital Stock—Unissued

Debit with:	Credit with:
(1)—Par value of preferred shares authorized.	(1)—Par value of preferred shares issued.

Balance—Represents the par value of shares unissued.

Common Capital Stock—Authorized

Debit with:	Credit with:
(1)—Par value of common shares retired.	(1)—Par value of common shares authorized.

Balance—Represents the par value of shares authorized.

Common Capital Stock—Unissued

Debit with:	Credit with:
(1)—Par value of common shares authorized.	(1)—Par value of common shares issued.

Balance—Represents the par value of shares unissued.

Surplus

Debit with:	Credit with:
(1)—Dividends declared by the board of directors. (2)—Net loss as shown by profit and loss account, after closing entries for the period have been made.	(1)—Amount of paid-in surplus. (2)—Appreciation of permanent assets. (3)—Net profit as shown by the profit and loss account, after closing entries for the period have been made.

Balance—Represents the accumulated net profits to and including the last closing period, less any dividends paid.

Undivided Profits

Debit with:	Credit with:
(1)—Extraordinary items of expenses and extraneous losses.	(1)—Items of extraordinary income and extraneous profits.
(2)—Balance of all expense accounts, and accounts showing losses, at each closing period.	(2)—Balance of all accounts showing income or profits, at each closing period.

Balance—Represents the net profit or loss for the period.

Investment
(Or Capital Accounts)

Debit with:	Credit with:
(1)—Withdrawals by partners, or sole proprietor.	(1)—Investment.
(2)—Extraordinary items of expenses or extraneous losses.	(2)—Items of extraordinary income or extraneous profits.
(3)—Expenses in connection with outside investments.	(3)—Interest allowed on investment.
(4)—Net loss as shown by profit and loss account, after closing entries for the period have been made.	(4)—Net income from outside investments.
	(5)—Salaries of partners, or sole proprietor, if a personal account is not kept.
	(6)—Net profit as shown by profit and loss account, after closing entries for the period have been made.

Balance—Represents the net investment, or capital, of each partner or sole proprietor.

Profit and Loss—Current Account

Debit with:	Credit with:
(1)—Balance of all expense accounts, and accounts showing losses, at each closing period.	(1)—Balance of all accounts showing income or profits, at each closing period.

Balance—Represents the net operating profit or loss for the period.

PART V

OPERATING ACCOUNTS

BOOKKEEPING PROCEDURE

The book entries are a very important factor in obtaining the desired results, and in this connection Chart number twenty-one, Volume II, and the following text will be of material assistance.

INCOME

(See also descriptive text accompanying items 2-7 inclusive of Operating Statement. Separate accounts should be maintained for leased sections).

Cash Sales

Debit with:	Credit with:
(1)—Balance of account "Returns and Allowances on Cash Sales." (2)—Balance transferred to Profit and Loss—Current Period.	(1)—Gross Cash Sales of merchandise. (2)—Gross Cash Sales of restaurant. (3)—Gross Cash Sales of personal service departments. (4)—Gross Cash Sales of alteration rooms.

Returns and Allowances
(Cash Sales)

Debit with:	Credit with:
(1)—Amounts refunded cash customers for merchandise returned. (2)—Amounts allowed cash customers on merchandise not returned.	(1)—Balance transferred to Cash Sales.

Charge Sales

Debit with:	Credit with:
(1)—Balance of account "Returns and Allowances on Charge Sales." (2)—Balance transferred to Profit and Loss—Current Period.	(1)—Gross Charge Sales of merchandise. (2)—Gross Charge Sales of restaurant. (3)—Gross Charge Sales of personal service departments. (4)—Gross Charge Sales of alteration rooms.

Returns and Allowances
(Charge Sales)

Debit with:	Credit with:
(1)—Amounts credited charge customers for merchandise returned. (2)—Amounts allowed charge customers on merchandise not returned.	(1)—Balance transferred to Charge Sales.

C. O. D. and Will Call
Or Layaway Sales

Debit with:	Credit with:
(1)—Balance of account "Returns and Allowances on C. O. D. and Will Call Sales." (2)—Balance transferred to Profit and Loss—Current Period.	(1)—Gross C. O. D. or Will Call Sales of merchandise. (2)—Gross C. O. D. or Will Call Sales of alteration rooms.

Returns and Allowances
(C. O. D. and Will Call or Layaway Sales)

Debit with:

(1)—Amounts refunded C. O. D. and WILL CALL customers for merchandise returned or credited them for merchandise not accepted.

(2)—Amounts allowed C. O. D. and WILL CALL customers on merchandise not returned.

Credit with:

(1)—Balance transferred to C. O. D. and WILL CALL Sales.

COST OF SALES

(See also descriptive text accompanying items 8–26 inclusive of Operating Statement).

Net Cost of Merchandise Sold

Debit with:

(1)—Gross cost of merchandise sold.

Credit with:

(1)—Balance transferred to Profit and Loss—Current Period.

Discount Earned on Merchandise Purchases

Debit with:

(1)—Amount transferred to special reserve account representing discount on inventory at end of period.

(2)—Balance transferred to Profit and Loss—Current Period.

Credit with:

(1)—Amount transferred from special reserve account representing discount on inventory at beginning of period.

(2)—Discounts earned on merchandise purchases during period.

Alteration Costs

Debit with:

(1)—Cost of materials used.

(2)—Wages.

(3)—Other Expenses.

Credit with:

(1)—Balance transferred to Profit and Loss—Current Period.

Merchandise Costs—Leased Departments

Debit with:

(1)—Cost of Leased Section Sales.

Credit with:

(1)—Balance transferred to Profit and Loss—Current Period.

EXPENSES

(See also descriptive text accompanying items 21–23 inclusive of Operating Statement, and Classification and Distribution of Expenses.

Operating Expenses

DEBIT WITH:	CREDIT WITH:
(1)—All operating expenses.	(1)—Amounts charged customers or others for expense incurred such as transportation charges to distant points. (2)—Transfers to Manufacturing Workroom, Alteration Rooms and Leased Sections. (3)—Balance transferred to Profit and Loss—Current Period.

OTHER INCOME AND LOSSES

(Accounts appropriate to any extraordinary operations of the business should be set up and closed out at the end of the period to Profit and Loss—Current Period). (See also descriptive text accompanying items 29–31 inclusive of Operating Statement).

PART V

CLASSIFICATION AND DISTRIBUTION OF EXPENSE

BOOKKEEPING PROCEDURE

In a small business, where detail is not desired, the expense accounts may be kept in the general ledger according to the Fourteen (14) Natural Divisions and closed to profit and loss at the end of the accounting period.

The larger business requires more detail and it is desirable, when the business is departmentized and expenses kept by the Fourteen Natural Divisions, grouped under the Five Functional Group Classifications, to maintain a subsidiary expense record, which balances with a single controlling account in the general or private ledger.

This subsidiary record should be divided so that the direct expenses can be charged direct to the selling departments and the indirect expenses to the service departments, but keeping the Five Functional Group Classifications intact. In posting items of Expense, the specific accounts in the subsidiary record should be debited with the separate items as they occur, and the totals of expense should be posted at periodic intervals, preferably monthly, to the controlling account in the general ledger. Chart number twenty-two, in Volume II, has been prepared so as to portray the source of information for expense distribution.

Expense accounts should be credited only with recoveries, made through the disposal of items previously charged to expense accounts. Receipts from salvage of items not charged to expense should not be credited to expense accounts.

If any of the service departments do work for other service departments, such as care of collectors' machines by the garage and automobile department, the latter should be credited through a Transfer Account (this account has not been provided in the Chart of Expense Accounts), and the account under credit offices charged. This transfer account should be only used for credits which consist of a consolidation of expenses covered by the charge, such as the one referred to above. Transfer of supplies or individual items should be credited to the account to which they were charged.

Alteration and Manufacturing expenses should be charged to their respective departments in a separate group under direct expenses. This group has been designated by the letter "W", so they can be segregated, being a charge to cost of sales and inventory, respectively.

At the end of the accounting period, the total of the expense account in the general ledger is transferred to Profit and Loss, thus automatically closing all the accounts in the subsidiary expense record.

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